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September 18, 1997

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

BY HAND DELIVERY

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W.
Room 222
Washington, D.C. 20554

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Re: Notice of Ex Parte Presentation; Federal-State - Joint Board on
Universal Service; CC Docket No. 96-45

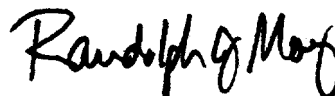
Dear Mr. Caton:

On September 18, 1997, the undersigned, representing EDS Corporation; John Lynn of EDS Corporation; Steve Stewart and Nat Clark of IBM, and Jack Nadler, representing the Information Technology Association of America, met with Diane Law and Lori Wright of the Common Carrier Bureau, to discuss certain aspects of the universal service fund as it relates to private operators, including systems integrators. The attached hand-outs, in addition to the pleadings of the above-referenced parties already filed in CC Docket No. 96-45, covers the points discussed at the meeting.

Pursuant to Section 1.1206(b) of the Commission's rules, an original and one copy of this letter and attachment are being filed with the Secretary. Please date stamp the "stamp and return" copy of the letter for return by the messenger.

If you have any questions concerning this submission, please contact the undersigned.

Sincerely,



Randolph J. May

Enclosure

cc: Diane Law, Common Carrier Bureau
Lori Wright, Common Carrier Bureau

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Ex Parte Submission of the Ad Hoc Telecommunications Users Group, EDS Corporation, the Information Technology Association of America, and International Business Machines Corporation, CC Docket 96-45

**THE COMMISSION SHOULD RECONSIDER ITS DECISION
TO IMPOSE UNIVERSAL SERVICE PAYMENT OBLIGATIONS
ON SYSTEMS INTEGRATORS
AND OTHER PRIVATE SERVICE OPERATORS**

- **Systems integrators support the goal of universal service. They will make contributions to universal service through the rates that they pay to common carriers for telecommunications services. However, requiring these providers to make direct payments to the universal service fund raises significant problems. This approach:**
 - would impose significant new costs, with no corresponding public interest benefits;
 - would impose a form of common carrier regulation on previously unregulated competitive operators;
 - would result in systems integrators making "double payments";
 - is inconsistent with congressional intent; and
 - could result in reduced services for business customers.
- **Requiring systems integrators to make payments to the universal service fund in the same manner as common carriers will impose significant new costs, while providing no new benefits.**
 - Systems integrators will incur significant costs.
 - + Unlike common carriers, systems integrators do not classify revenue as telecommunications or non-telecommunications. Nor do they separate interstate and intrastate revenues.
 - + To comply with the Order, systems integrators will be required to fundamentally restructure their business operations to reflect these regulatory distinctions.

- + This will impose far more significant costs than the Commission anticipated. For some firms, these costs may outweigh the size of their USF payments.
 - Requiring systems integrators to make payments to the USF will not generate any additional revenue for universal service, and will have almost no effect on the size of the carriers' contributions.
- **Requiring systems integrators to make payments directly to the universal service fund would extend a form of common carrier regulation to competitive, previously non-regulated businesses.**
 - The Order, for the first time, imposes identical regulatory obligations on common carriers and private service operators -- an outcome clearly at odds with the deregulatory policies that Congress embodied in the Telecommunications Act.
 - Imposing USF payment obligations on private service operators could encourage and facilitate imposition of other forms of common carrier regulation by State and foreign regulatory authorities.
- **Requiring systems integrators to make payments directly to the universal service fund would not be competitively neutral; it will result in double counting**
 - Requiring system integrators to make payments to the USF is not necessary to promote competitive neutrality.
 - + Systems integrators do not compete against common carriers by providing stand-alone telecommunications services.
 - + Rather, they offer service packages that may include consulting, network design and management, enhanced services, data processing, software applications, and computers and customer premises equipment.
 - + Telecommunications typically is an incidental part of a systems integrator's offerings.

- In any case, the payment mechanism adopted in the Order is not competitively neutral. Rather, it will result in systems integrators making "double payments" to the USF.
 - + Contrary to the Commission's assumption, because of the existence of long-term contracts, common carriers will not provide capacity to systems integrators at discounted rates.
 - + Systems integrators, however, will be required to make payments to the USF on all transactions involving telecommunications.
 - + At the same time, systems integrators will not be able to pass these costs on to their customers.
- **The Commission's imposition of universal service payments on non-carriers, including systems integrators, violates congressional intent.**
 - The Telecommunications Act expressly preserves the distinction between common carriers and private service operators.
 - Congress permitted the Commission to require private service operators to make USF payments if the agency determined that network bypass threatens the fund.
 - The Commission has made no finding regarding bypass. Rather, it concluded that -- in the interest of "competitive neutrality" -- private service operators should be treated the same as common carriers. The FCC cannot substitute its judgment for that of the Legislature.
- **Solution I: Limit the universal service fund payment obligation to common carriers.**
 - This approach would eliminate all legal, policy, and administrative issues.
 - This is the approach originally proposed in the House bill and by the Joint Board.

- **Solution II: Do not require systems integrators to make direct payments to the universal service fund.**
 - Because systems integrators typically do not compete against common carriers, the principle of competitive neutrality does not require that they contribute to the USF.
 - Systems integrators can be readily distinguished from carriers and other "other telecommunications providers."
 - This approach would not require major change to the Order.

- **Solution III: Modify the Order to eliminate the "double counting" problem.**
 - There are at least three ways in which the Commission could eliminate the double counting problem:
 - + replace the end-user revenue approach with a "net telecommunications revenue" methodology;
 - + require carriers to provide lower rates to systems integrators and other private service operators that reflect the "avoided cost" from not having to make USF contributions based on telecommunications revenues obtained from these entities;
 - + require carriers to provide systems integrators and other private service operators with a "fresh look" at existing telecommunications contracts.
 - While this approach would provide important relief for the near to intermediate term, it would not resolve the long-term legal, policy, and administrative issues.

- **At a minimum, the Commission should limit the January 1998 universal service fund payment obligation to common carriers, and issue a further notice of proposed rulemaking.**
 - Imposition of USF payment obligation on systems integrators and other private service operators has raised numerous legal, policy, and administrative issues that the Commission did not anticipate.
 - The Commission should release a further notice of proposed rulemaking in order to develop a more adequate record regarding the imposition of USF payment requirements on non-carriers, including systems integrators.
 - This approach will not reduce the amount of money available for universal service, and will have a de minimis effect on the size of carriers' initial USF payments.
 - Pending further action by the Commission, non-carriers would contribute to universal service through payments to their carriers.

Ex Parte Submission of the Ad Hoc Telecommunications Users Group, EDS Corporation, the Information Technology Association of America, and International Business Machines Corporation, CC Docket 96-45

THE COMMISSION SHOULD RECONSIDER ITS DECISION TO IMPOSE UNIVERSAL SERVICE PAYMENT OBLIGATIONS ON SYSTEMS INTEGRATORS

WHAT ARE SYSTEMS INTEGRATORS?

Systems integrators are providers of managed data processing and information services packages that may include network design and management, information and enhanced services, computers and customer premises equipment, data processing, and software applications. Systems integrators may provide telecommunications to third parties: (1) as an incidental part of their integrated offering, and not on a stand-alone basis; (2) over facilities provided by common carriers; and (3) pursuant to individually negotiated private contracts.

DOESN'T THE PRINCIPLE OF "COMPETITIVE NEUTRALITY" REQUIRE THAT SYSTEMS INTEGRATORS MAKE DIRECT PAYMENTS TO THE UNIVERSAL SERVICE FUND?

The Commission's concern about competitive neutrality is not applicable to systems integrators because systems integrators do not compete against providers of stand-alone telecommunications services. In antitrust terms, "systems integration" and "telecommunications" services are not in the same relevant market. Customers do not view systems integration services as a substitute for telecommunications. See Department of Justice-Federal Trade Commission Merger Guidelines § 1.11. Indeed, it would not be economically rational for a customer to contract with a systems integrator solely to obtain telecommunications. Consequently, neither telecommunication providers nor systems integrators "base business decisions on the prospect of buyer substitution between [these services] in response to changes in price or other competitive variables." Id.

HOW ARE SYSTEMS INTEGRATORS DIFFERENT FROM OTHER PARTIES THAT ARE REQUIRED TO MAKE DIRECT PAYMENTS TO THE UNIVERSAL SERVICE FUND?

Systems integrators can be readily differentiated from other entities who will be required to make direct payments to the USF. Unlike telephone companies, systems integrators do not own telecommunications facilities. And, unlike resellers, they are not common carriers. Rather, systems integrators are a type of enhanced service providers. The fact that these operators provide incidental telecommunications as an incidental part of their integrated offering does not alter the enhanced status of the entire offering. See Amendment to Section 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry), Phase II Reconsideration Order, 3 FCC Rcd 1150, 1170 n.23 (1988) (subsequent history omitted). Under the Telecommunications Act, firms may not be required to contribute based on revenues from enhanced services.

WHAT IMPACT WOULD THIS HAVE ON THE UNIVERSAL SERVICE FUND?

Virtually none. The size of the USF will remain the same. Moreover, eliminating the requirement that systems integrators make direct payments to the USF would have almost no impact on the size of the carriers' USF payments. While precise data is not available, we estimate that carrier contributions would increase by no more than one-quarter of one percent. At the same time, systems integrators will make significant contributions to universal service through the rates they pay to the facilities-based carriers from which they obtain service.